

Update



NATIONAL ASSOCIATION OF REAL ESTATE INVESTMENT TRUSTS®

In this issue:

• FASB - page 1

- Proposes Guidance for Determining Whether Operating Segments May be Aggregated
- EITF Considers Partnership Consolidation Rules That Could Increase Consolidation of Joint Ventures
- Contemplates Adding PP&E Related Topics to its Agenda
- Issues Final Guidance on Conditional Asset Retirement Obligations

• SEC - page 3

- Gives Six Months Reprieve for Adopting FASB Statement No. 123(R) on Employee Stock Options
- Releases Staff Accounting Bulletin Regarding Stock Option Accounting
- Issues Final Rule on XBRL and Updates EDGAR Filer Manual
- Hosts Roundtable on SARBOX Section 404
- Issues Letter Regarding a Lessee's Accounting for Leases

• NAREIT - page 5

- Comments on SEC's Securities Reform Proposal
- Over 1,000 Industry Participants Attend the 2005 Law & Accounting Conference

FASB

Proposes Guidance for Determining Whether Operating Segments May be Aggregated

Under current accounting practices established by the Financial Accounting Standards Board's (FASB) Statement No. 131, an enterprise is permitted to aggregate two or more operating segments into a single operating segment only if the operating segments have similar economic characteristics.

Since the issuance of the Statement, companies have asked if both quantitative and qualitative factors should be considered for purposes of determining whether the economic characteristics of two or more operating segments are similar. In a recently proposed FASB Staff Position (FSP), the FASB staff believes both quantitative and qualitative factors should be considered for purposes of determining whether the economic characteristics of two or more operating segments are similar. Quantitative factors could include performance measures such as gross margins, trends in sales growth, returns on assets employed, and operating cash flows. Qualitative factors could include nonperformance measures such as competitive and operating risks, currency risks, as well as economic and political conditions associated with each segment.

We had requested NAREIT member companies to review this FSP and advise us if this would change the way segments are aggregated. To date we have not heard any significant concerns raised by members. [CLICK HERE](#) to access the FSP.

EITF Considers Partnership Consolidation Rules That Could Increase Consolidation of Joint Ventures

As reported in the December 2004 *Financial Standards Update*, on Dec. 23, 2004, the FASB's Emerging Issues Task Force (EITF) issued for comment, draft abstract EITF Issue 04-5, "*Investor's Accounting for an Investment in a Limited Partnership When the Investor Is the Sole General Partner and the Limited Partners Have Certain Rights.*" Click [HERE](#) to access the draft abstract.

NAREIT's comment letter dated Feb. 19, 2005, requested that the EITF consider a minimal economic interest threshold for its basic premise that a sole GP is presumed to control that limited partnership and therefore should consolidate the partnership. Additionally, NAREIT requested that the 20 percent rule contained in Example 1 of the abstract be eliminated and that the accounting rely on the preparer's and auditor's judgments as to whether acquisitions/dispositions and other transactions requiring approval of the limited partners are "in the ordinary course" of a partnership's business. Click [HERE](#) to access NAREIT's comment letter.

At the March 2005 meeting, the EITF concluded that no minimal economic interest threshold should be required for consolidation. Further, the EITF reaffirmed its prior tentative conclusion that a sole general partner is presumed to control a limited partnership and should consolidate the limited partnership unless: 1) the limited partners possess substantive kick-out rights as defined in

paragraph B20 of FIN 46(R), "*Consolidation of Variable Interest Entities;*" or 2) the limited partners possess substantive participating rights similar to the rights described in Issue 96-16, "*Investor's Accounting for an Investee When the Investor has a Majority of the Voting Interest but the Minority Shareholder or Shareholders Have Certain Approval or Veto Rights.*" In addition, the EITF agreed to expand the guidance to all limited partnerships, including those with multiple general partners.

However, the EITF tentatively agreed with NAREIT's second comment and eliminated the 20 percent of assets "bright line" threshold for evaluating whether the limited partner's right to block certain acquisitions and dispositions is a participating right or a protective right. The EITF concluded that this threshold should be replaced with an evaluation of whether the acquisitions and dispositions requiring the limited partner's approval are in the partnership's normal course of business.

The revised abstract is expected to be discussed and finalized at the June 2005 EITF meeting.

Contemplates Adding PP&E Related Topics to its Agenda

In February 2004, the FASB considered whether to add projects to its agenda, based on recommendations from the AICPA's Accounting Standards Executive Committee (AcSEC), on the following PP&E topics:

1. Accounting for planned major maintenance activities
2. Accounting for rental costs incurred during construction
3. Accounting for liquidated damages
4. The threshold for beginning to capitalize PP&E

During its revisions of the AICPA Airline Audit Guide, AcSEC noted that there are four methods of accounting for planned major maintenance activities: direct expensing, built-in overhaul, deferral and accrual. AcSEC requested that the Board add a project to its agenda to develop an FSP on accounting for planned major maintenance activities that would be applicable to all industries. The Board did not reach a decision about whether to add the topic to its agenda. Rather, the Board asked the FASB staff to complete additional research and return to the Board with a definition of what will be addressed and how the project's scope could be limited.

The FASB staff recommended, and the Board agreed, not to add topics 2, 3 and 4 to the Board's agenda.

Issues Final Guidance on Conditional Asset Retirement Obligations

In March 2005, the FASB issued FASB Interpretation No. 47, "*Accounting for Conditional Asset Retirement Obligations*" (FIN 47). Click [HERE](#) for the full text. FIN 47 clarifies that an entity must record a liability for a "conditional" asset retirement obligation if the fair value of the obligation can be reasonably estimated. The types of asset retirement obligations that are covered by this interpretation are those arising from an asset retirement activity which an entity has a legal obligation to perform, however the timing and (or) method of settling the obligation are conditional on a future event that may or may not be within the control of the entity. One example of such an obligation is a legal obligation to handle and dispose of asbestos in a special manner if and when asbestos-containing facility undergoes major renovations or is demolished. FIN 47 also clarifies when an entity would have sufficient information to reasonably estimate the fair value of an asset retirement obligation.

FIN 47 is effective for the Dec. 31, 2005 year end for most NAREIT member companies.

SEC

Gives Six Months Reprieve for Adopting FASB Statement No. 123(R) on Employee Stock Options

On Apr.14, 2005, the Securities and Exchange Commission (SEC) adopted a new rule that amends the compliance dates for FASB's Statement No. 123(R), "*Share-Based Payment (Statement No. 123R)*". Under Statement No. 123R, most NAREIT members would have been required to implement the standard during the 3rd Quarter of 2005. The Commission's new rule allows companies to implement Statement No.123R at the beginning of their next fiscal year, instead of the next reporting period, that begins after June 15, 2005. This means, that the financial statements for a calendar year-end company do not need to comply with Statement No. 123R until the interim financial statements for the first quarter of 2006 are filed with the Commission. Click [HERE](#) to access the SEC press release.

Releases Staff Accounting Bulletin Regarding Stock Option Accounting

On Mar. 29, 2005, the SEC's Office of the Chief Accountant and its Division of Corporation Finance announced the release of a Staff Accounting Bulletin relating to the FASB's accounting standard for stock options and other share-based payments. The interpretations in Staff Accounting Bulletin No. 107, "*Share-Based Payment,*" (SAB 107) express views of the SEC staff regarding the application of Statement No.123R. Click [HERE](#) to access the full text of SAB 107.

Statement No.123R was issued by the FASB on Dec. 16, 2004. Among other things, SAB 107



provides interpretive guidance related to the interaction between Statement No.123R and certain SEC rules and regulations, as well as provides the staff's views regarding the valuation of share-based payment arrangements for public companies. The SEC does not prescribe any particular valuation model. SAB 107 also reminds public companies of the importance of including disclosures within filings made with the SEC relating to the accounting for share-based payment transactions, particularly during the transition to Statement No.123R.

The SEC staff believes the interpretive guidance in SAB 107 will assist both public entities in applying the provisions of Statement No.123R and investors and other users of financial statements in analyzing the information provided under that Statement. The statements in SABs are not rules or interpretations of the Commission, nor are they published as bearing the Commission's official approval. They represent interpretations and practices followed by the Office of the Chief Accountant and the Division of Corporation Finance in administering the disclosure requirements of the federal securities laws.

Issues Final Rule on XBRL and Updates EDGAR Filer Manual

In February 2004, the SEC issued a final rule adopting amendments to establish a voluntary program related to eXtensible Business Reporting Language (XBRL). Registrants may voluntarily furnish XBRL data in an exhibit to specified filings under the Securities Exchange Act of 1934 and the Investment Company Act of 1940. The program begins with the 2004 calendar year-end reporting season. Click [HERE](#) to access the final rule.

XBRL is a royalty-free, universal information-format standard that enables all software to share and process business information using Internet

technology, such as the Web services standards. Since they are software- and platform-neutral, XBRL and Web services can be deployed over existing company systems to automate information exchange-creating a straight-through reporting environment. This eliminates manual information gathering and consolidation tasks, pulls time and costs out of internal reporting processes, enables reporting or analytical software to instantly re-use information and benefits management's decision-making process.

In addition, the SEC adopted revisions to the Electronic Data Gathering, Analysis, and Retrieval System (EDGAR) Filer Manual to support the voluntary submission of tagged financial information using XBRL. Click [HERE](#) to access the final rule.

Hosts Roundtable on SARBOX Section 404

On Apr. 13, 2005, the SEC hosted a roundtable discussion and solicited written feedback regarding the experiences of registrants, accounting firms and others in implementing the new internal control requirements under Section 404 of the Sarbanes-Oxley Act of 2002. In order to solicit feedback from member companies, NAREIT hosted a conference call on Mar. 15, 2005. Nearly 25 member companies participated on the call and based on member feedback, NAREIT submitted a comment letter to the SEC. Click [HERE](#) to access NAREIT's comment letter.

Many of the comments/concerns raised by NAREIT in its letter were echoed by the participants. All participants agreed that the costs of implementing and complying with the Section 404 requirements have far exceeded the expectations. The participants suggested that the final implementation of the SEC's accelerated reporting deadlines be reconsidered and remain at 75 days after fiscal year-end and 40 days after quarter year-end. Additionally, the participants suggested that the reporting and remediation

requirements be modified based on a higher threshold level, i.e. controls that would “likely” result in material misstatements.

Issues Letter Regarding a Lessee’s Accounting for Leases

On Feb. 7, 2005, the SEC issued a letter to the AICPA that provides the SEC’s views on a lessee’s/tenant’s accounting for three items that can be found in operating leases. The SEC’s views focused on a tenant’s accounting for: 1) the amortization of leasehold improvements; 2) “rent holidays”— periods of free rent while the tenant has possession of the space and, 3) incentives related to leasehold improvements, including landlord reimbursements to the tenant for the tenant’s cost of improvements to the space. To emphasize, this SEC letter did not explicitly address the lessor’s/landlord’s accounting for these items. Click [HERE](#) to access the letter.

Since the issuance of the SEC letter, more than 200 lessees/tenants have restated their financial statements for one or more of the issues addressed in the SEC letter, in addition to other accounting issues. As a result of these restatements, some of the lessees/tenants have capitalized the costs of improvements to the space to be occupied on their books, which our members have historically recorded and continue to record on their books as tenant improvement assets. These lessee restatements have caused considerable confusion and concern with respect to whether the lessor/landlord or the lessee/tenant should report these space improvements as property on its books. The SEC letter did not provide explicit guidance on this question. However, the SEC letter indicated that, “the staff recognizes that evaluating when improvements should be recorded as assets of the lessor or assets of the lessee may require significant judgment and factors in making that evaluation are not the subject of this letter.”

Based on input from our members, as well as the major accounting firms, we have requested that the EITF provide guidance on the factors that should be considered in making this determination as to who, the landlord/lessor or the tenant/lessee, should record a tenant improvement/property asset on their books. Click [HERE](#) to access NAREIT’s letter to the EITF.

NAREIT

Comments on SEC’s Securities Reform Proposal

In October 2004, the SEC proposed major amendments to the registered offering framework under the Securities Act of 1933. If adopted, the proposal would result in rule changes in the areas of communications, registration procedures, the timing of disclosures proved to investors and liability issues. NAREIT’s comment letter dated Jan. 31, 2005, commended the SEC’s efforts to continue to promulgate high-quality rules and requirements that intend to modernize the securities offering process and that provide more timely information to investors. Click [HERE](#) to access NAREIT’s comment letter.

Overall, we supported the requirements in the proposal. However, we urged the SEC to consider the prevalent UPREIT structure in the context of defining “well-known seasoned issuers.” Additionally, we requested that the SEC provide a specific exemption permitting UPREITs (or any corporate owned partnership that has the same structure as an UPREIT) to utilize a prospectus supplement in connection with identifying selling security holders under an evergreen shelf registration statement. Click [HERE](#) to access the complete SEC proposal.

Over 1,000 Industry Participants Attend the 2005 Law & Accounting Conference

NAREIT's Law & Accounting Conference was held from Apr. 6 through Apr. 8, 2005 in Washington, D.C. at the J.W. Marriott Hotel. NAREIT thanks Esther Blum of Taubman Centers, Eric Kevorkian of Boston Properties, Tom Robinson of Legg Mason Wood Walker and Jim Sowell of Deloitte & Touche for serving as program directors. The conference was very successful and attended by more than 1,000 NAREIT members. Members included executives and staff from REITs, as well as accountants, lawyers and professionals who service the industry. The program provided a broad range of learning experiences. Sessions covered recently issued and proposed accounting standards, the new corporate governance and financial reporting environment, the current capital markets and best practices with respect to financial reporting.

Of special interest to many attendees was the International Financial Standards session. In addition to learning about the work and agenda of the Internal Accounting Standards Board (IASB) and the FASB's convergence process, attendees were made aware of the International Valuation Standards Committee, its standards and its work with the IASB. The 2005 edition of these valuation standards is available by clicking [HERE](#).

At the Accounting Committee meeting, Sandy Blum and Tom Wilkin of PricewaterhouseCoopers presented their firms' views on the proposed guidance on business combinations, as well as the SEC's letter related to the accounting for leases. Jenni Sullivan from the FASB provided an overview of the joint FASB/IASB Performance Reporting project.



NAREIT

Steven A. Wechsler
President and CEO

(202) 739-9400, swechsler@nareit.com

Financial Standards/SEC Team

Tony M. Edwards

Senior Vice President and General Counsel

(202) 739-9408, tedwards@nareit.com

George L. Yungmann

Vice President, Financial Standards

(202) 739-9432, gyungmann@nareit.com

Gaurav Agarwal

Director, Financial Standards

(202) 739-9442, gagarwal@nareit.com